



Reversal of Impairment Losses on Participations

April 2020

The asymmetrical treatment of capital gains and losses from participations was already repealed from Liechtenstein tax law in 2018¹. Transitional provisions still ensure the taxation of the reversal of impairment on value-adjusted participations in the future. Now a possibility has been created for the early reversal of impairment losses on portfolio participations. This newsletter highlights in particular the reversal of impairment losses using the regular and simplified procedure.

Tax Treatment of Capital Gains and Losses from Participations in Liechtenstein

In principle, capital gains from participations are treated as tax-neutral in Liechtenstein. This means that realized capital gains (price gains) from sale or liquidation as well as unrealized increases in value of participations in legal entities generally represent tax-exempt corporate income.

By contrast, losses (price losses) from participations could be asserted as tax-effective up to and including the 2018 tax year. In the event of a permanent or realized depreciation of the participation, it was possible to make a write-down or value adjustment which was considered a tax-deductible expense.

Up to the 2018 tax year	
Capital gains from participations	Losses from participations
Tax-neutral (tax-exempt income)	Tax-effective (tax-deductible expense)

This asymmetrical tax treatment of capital gains and losses from participations was criticized by the EU in the course of compiling the EU list of non-cooperative jurisdictions for tax purposes. Liechtenstein then ad-

justed its tax law² and repealed the deductibility of losses from participations (Art. 53 of the Tax Act [SteG], old version).

From the 2019 tax year both capital gains and losses from participations are treated as tax-neutral. Realized capital gains and unrealized value increases of participations in legal entities are deemed, subject to the anti-abuse provisions, tax-exempt corporate income (Art. 48 (1) (f) of the Tax Act). Realized and unrealized losses from participations are no longer tax-deductible and are now part of the taxable corporate income (Art. 47 (3) (c^{bis}) of the Tax Act).

From the 2019 tax year	
Capital gains from participations	Losses from participations
Tax-neutral (tax-exempt income)	Tax-neutral (non-tax-deductible expense)

The tax neutrality of the new legal situation is illustrated by the numerical example on page 2. The write-down or value adjustment on participation 1 that was accepted for tax purposes up to and including the 2018 tax year is corrected from the 2019 tax year and added to the taxable corporate income. In the following, highly simplified example, the taxable net corporate income, on which the corporate income tax is ultimately levied, corresponds to the profit determined under commercial law before valuation adjustments.

If the tax exemption for capital gains and unrealized value increases is denied due to the new anti-abuse provision (Art. 48 (6) of the Tax Act), realized and unrealized losses from these participations are nonetheless not accepted as tax-deductible. This can be justified by the fact that realized and unrealized losses from

¹ Act of June 7, 2018 on the Amendment of the Tax Act, Law Gazette 2018 No. 147.

² See CONFIDA Info "[Amendment of the Tax Act in Liechtenstein](#)" from May 2018.

	Up to the 2018 tax year		From the 2019 tax year	
	Commercial law	Tax law	Commercial law	Tax law
Profit before valuation adjustments	100		100	
Write-down on participation 1	-10		-10	
Value increase of participation 2	5		5	
Profit	95	95	95	95
Tax correction: write-down on participation 1		-		+10
Tax correction: value increase of participation 2		-5		-5
Taxable net corporate income		90		100

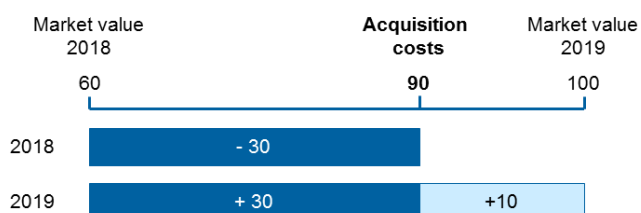
participations are generally to be treated as tax-neutral. In the case of realized and unrealized capital gains from participations with low-taxed passive income, there is a deviation from the principle of tax neutrality to subject these capital gains to "regular taxation" in order to prevent abuse.

Tax Treatment of Reversals of Impairment Losses

Due to the tax neutrality of losses from participations applicable from the 2019 tax year, the appreciation in value (reversals of impairment losses under commercial law) is consequentially also to be treated as tax-neutral. The value adjustments on participations that have been dissolved in an income-effective manner under commercial law are generally no longer tax-effective and must be corrected accordingly for tax purposes (deducted from the profit determined under commercial law).

For reversals of write-downs on or value adjustments of participations asserted for tax purposes up to and including the 2018 tax year, transitional provisions to the repealed Art. 53 of the Tax Act were provided. Accordingly, if the reasons for the permanent value impairment cease to exist, a tax effective write-up must be made. If the write-downs and/or value adjustments carried out up to and including the 2018 tax year in a tax-effective manner are reversed under commercial law, the reversal of impairment generally represents taxable income.

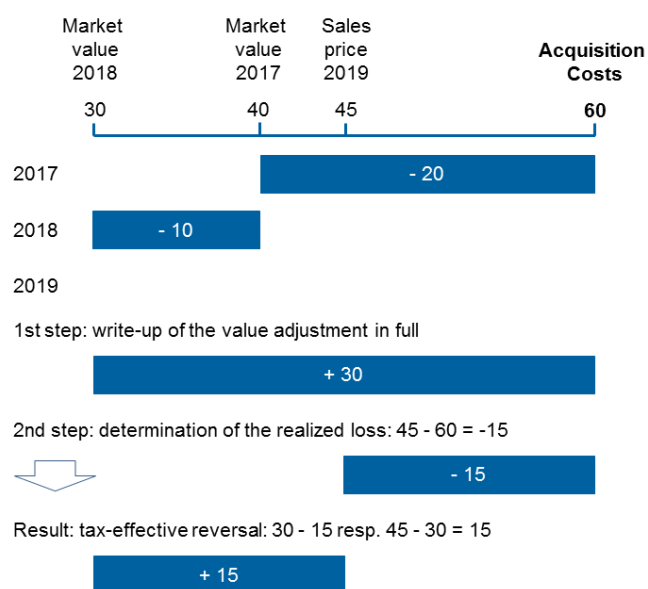
The amount of the tax-effective write-up is limited to the amount of the previously made write-down or value adjustment. If a participation is revalued above its acquisition costs, the reversal of impairment is tax-effective up to the acquisition costs (taxable corporate income); the revaluation above acquisition costs is tax-neutral (tax-exempt corporate income).



Reversals of Impairment Losses using the Regular Procedure

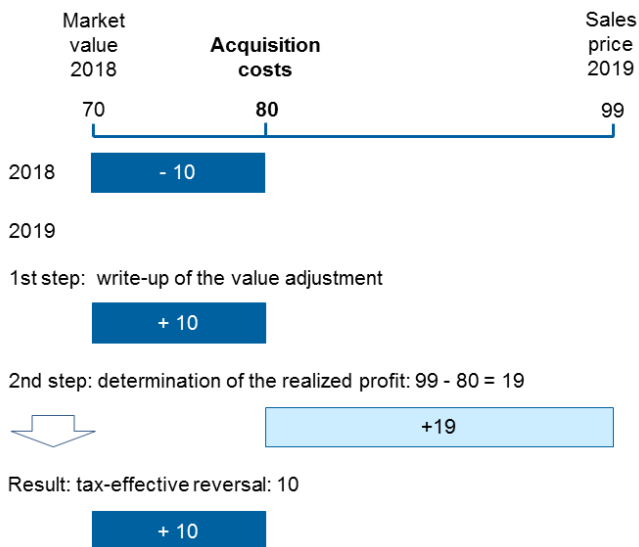
The value adjustments from the tax years up to and including 2018 are to be determined separately for each participation and continued annually up to the full reversal.

When participations are sold, the write-downs that were once tax-effective must also be reversed for tax purposes in a tax-effective manner. If the sales price is below the acquisition costs, there is a tax-effective write-up up to a maximum of the realized net accounting profit. According to administrative practice³, this procedure must be shown in the tax return by using gross amounts. In a first step, the value adjustment has to be reversed in full in a tax-effective manner. In a second step, the amount of the realized profit or loss (sales price minus the acquisition costs) must be determined. In the following example there is a realized loss of -15. As a result, the two steps lead to a realized net accounting profit of +15, which corresponds to the tax-effective reversal of impairment loss.



³ Information leaflet on the implementation of Section 3 of the Transitional Provision to Art. 53 of the Tax Act and Art. 49a of the Tax Ordinance regarding the reversal of impairment losses on participations, March 2020.

If the sales price is above the acquisition costs of the participation, all value adjustments must first be written up in a tax-effective manner, up to the amount of the acquisition costs. In the second step, the realized profit is determined (sales price minus acquisition costs). In the following example, the realized net accounting profit (sales price minus book value; 99 - 70 = 29) consists of the tax-effective reversal of impairment of 10 and the tax-neutral or tax-exempt profit from the sale of the participation of 19.



Reversals of Impairment Losses on Portfolio Participations

The regular procedure has the advantage that the reversals of impairment losses reflect the actual circumstances, but this procedure is quite intricate for the taxpayer. In order to simplify the administration, a possibility for portfolio participations was created to make the reversal of value adjustments prematurely. According to Art. 49a of the Tax Ordinance, tax-effective write-ups can be made on request even without the absence of reasons for permanent impairment. However, this only applies to participations of less than 10% in the capital of the legal person. If the simplified procedure is chosen, all portfolio participations must be included.

The value of the tax-effective reversal of impairment losses is determined as follows:

Balance of impairments at the end of 2018 (on all portfolio participations)
- 10%
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= Reversal-of-impairment amount
÷ 3 (years)
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= Tax-effective reversal of impairment losses for 2019, 2020 and 2021

The balance of value adjustments (balance of impairment losses or balance from unrealized price losses) on all portfolio participations at the end of the 2018 tax year minus a 10% reduction results in the tax-relevant reversal-of-impairment amount, which is written up over the 2019, 2020 and 2021 tax years.

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